

Risky Private Student Lending on the Rise Again

December 22, 2011

The private student loan market is showing clear signs of growth after increasing at double-digit rates through the late 1990s and early 2000s and then abruptly falling as a result of the 2008 financial market crisis.¹ Private loans are not a form of financial aid and are among the riskiest ways to pay for college. Private student lenders are not required to provide the important borrower options and protections that come with federal student loans, such as unemployment deferments, income-based repayment, public service loan forgiveness, and cancellation if the borrower dies, is severely disabled or is defrauded by a school. Like credit cards, private loans typically have variable, uncapped interest rates and offer little, if any, repayment flexibility. But unlike credit cards, private loans are virtually impossible to discharge in bankruptcy.² **Nevertheless, at the peak of the private loan market in 2007-08, a majority of private loan borrowers could have borrowed more in safer, more affordable federal student loans.**³

The many signs of renewed growth in the private loan market include:

- **Largest private lenders report growth.** Sallie Mae, the largest private lender, recently reported a 20% increase in loan originations so far this year and a 29% increase in loan originations in the third quarter of 2011 alone.⁴ Wells Fargo has been reporting growth in private loan volume every quarter for the last two years.⁵ Discover Financial, which recently acquired Citibank's private loan business, saw their private loan portfolio grow more than three times as much in the most recent quarter as compared to the same time last year.⁶
- **Private lenders have resumed lending to students at for-profit colleges.** In March 2011, Education Management Corporation, the second-largest for-profit college corporation, announced it was ending its institutional lending program, which it had started in 2008 when its students were having trouble getting loans. It reports that is no longer a problem: "We no longer believe the program is needed."⁷
- **Largest private lender loosens lending standards.** A *Wall Street Journal* article reported that in 2010 Sallie Mae's Chief Executive Officer thought the company may have become too restrictive in its lending practices and that "volumes should pick back up as the company did some 'tweaking' to its standards."⁸

¹ The Institute for College Access & Success' Project on Student Debt. *Critical Choices: How Colleges Can Help Students and Families Make Better Decisions about Private Loans*. July 2011. http://ticas.org/files/pub/critical_choices.pdf. Student Lending Analytics. "This Week in Financial Literacy: Private Student Loan Growth at Sallie Mae, Fed Data Shows Persistently High Delinquency Rates." *Student Lending Analytics Blog*. October 23, 2011. http://studentlendinganalytics.typepad.com/student_lending_analytics/2011/10/this-week-in-financial-literacy-.html.

² Testimony of Lauren Asher before the Subcommittee on Commercial and Administrative Law of the House of Representatives Committee on the Judiciary. Hearing entitled, "An Undue Hardship? Discharging Educational Debt in Bankruptcy." September 23, 2009. <http://judiciary.house.gov/hearings/pdf/Asher090923.pdf>.

³ The Project on Student Debt. *Private Loans: Facts and Trends*. July 2011. http://projectonstudentdebt.org/files/pub/private_loan_facts_trends.pdf.

⁴ Sallie Mae. "Sallie Mae reports third-quarter financial results: Loan originations up 29 percent compared to year-ago quarter." October 19, 2011. <http://bit.ly/uEuA4d>.

⁵ Wells Fargo & Company quarterly earnings supplements for 2010 and 2011. https://www.wellsfargo.com/invest_relations/earnings.

⁶ Analysis of U.S. Securities and Exchange Commission. 10-Q and 10-K filings for 2010 and 2011 for Discover Financial Services.

⁷ Malloy, Daniel. "EDMC ends loans during tough times for industry: Credit still tight for students at for-profits." *Pittsburgh Post-Gazette*. March 20, 2011. <http://www.post-gazette.com/pg/11079/1133033-28.stm#ixzz1HBp2CrEP>.

⁸ Korn, Melissa. "Sallie Mae Cuts Private-Loan Rates to Maintain Volume Growth." *The Wall Street Journal*. May 16, 2011. <http://on.wsj.com/jqTBAj>.